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No. 83-244

In the Supreme Court of the United States

OCTOBER TERM, 1983

TELEGRAPH SAVINGS AND LOAN ASSOCIATION, ET AL.,
PETITIONERS

v.

WILLIAM J. SCHILLING, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly concluded that the statutory requirements (12 U.S.C. 1729(c)(2)(A), (B) and (C)) for the appointment of a federal receiver for a state-chartered savings and loan association had been satisfied.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3-23 is reported at 703 F.2d 1019. The opinions of the district court (Pet. App. 24-86) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on March 29, 1983 (Pet. App. 23). A petition for rehearing was denied on May 12, 1983 (Pet. App. 2).

The petition for a writ of certiorari was filed on August 10, 1983. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case arises from the appointment of the Federal Savings and Loan Insurance Corporation ("FSLIC") as federal receiver for petitioner Telegraph Savings and Loan Association ("Telegraph"), a state-chartered savings and loan association. The district court held that the Federal Home Loan Bank Board ("Bank Board")[1] complied with the statutory requirements of 12 U.S.C. 1729(c)(2)(A), (B) and (C) when it appointed FSLIC as federal receiver. The Seventh Circuit affirmed, concluding that these requirements had been satisfied and that the statute was constitutional on its face and as applied to petitioners (Pet. App. 19-21).

2. Telegraph had experienced serious financial difficulties for more than a year before it was closed. It was dangerously under-capitalized (Pet. App. 4, 69) and, by mid-1979, failed to satisfy federal reserve and net worth requirements. *Id.* at 32, 68; see 12 U.S.C. 1726(b); 12 C.F.R. 563.13. Between June

[1] The Bank Board is an independent agency of the Executive Branch of the United States that is responsible, pursuant to Section 5 of the Home Owners' Loan Act of 1933, 12 U.S.C. 1464, for the "organization, incorporation, examination, operation, and regulation" of federal savings and loan associations. 12 U.S.C. 1464(a). The Bank Board is also the operating head of FSLIC, the corporate governmental agency of the United States that is responsible, pursuant to Title IV of the National Housing Act, 12 U.S.C. 1724-1730, for insuring the accounts of all federally-chartered savings and loan associations and most state-chartered savings and loan associations.

1979 and May 22, 1980, Telegraph incurred substantial and increasing operating losses, month after month (Pet. App. 4, 32, 67-70). By May 22, 1980, according to calculations by petitioners' two most senior financial officers, it was insolvent (*id.* at 42, 69-70, 82). No matter how its assets were valued, Telegraph's obligations to depositors and creditors exceeded the value of its remaining assets. *Id.* at 37 n.6, 41-42.

Telegraph's financial performance was far worse than that of other savings and loan associations in its geographic area. Telegraph's own Operating Report and statistical information supplied by the Federal Home Loan Bank of Chicago showed the net loss of savings for March 1980 to be 295% larger than that of comparable associations in the region. Def't Exh. 16. The same report showed that Telegraph's losses in earnings for the past 12 months placed it 447% behind comparable local associations (Pet. App. 49-50 n.14). And Telegraph's losses in earnings for the most recent month placed it 990% behind (*ibid.*). As these losses mounted, Telegraph continued to hold $5,000,000 of deposits in excess of FSLIC's insurance limit of $100,000 per account; it thus had a substantial number of depositors whose accounts were uninsured and who risked losing their savings. Affidavit of Bernard J. Conover at Exh. 15.

The Illinois Commissioner of Savings and Loan Associations and federal regulatory authorities attempted repeatedly to persuade Telegraph's owners to contribute additional funds to prevent its failure and to protect the depositors. Pet. App. 69-70; Deposition of William J. Schilling at 169-173. Twice during 1979, and again in March 1980, special meetings of Telegraph's board were called by regulatory authorities to urge the association to solve its problems.

Pet. App. 69. Regulatory authorities made a specific request that Telegraph's owners infuse $2,000,000 of new capital, but the owners refused. Deposition of William J. Schilling at 169-173. The best alternative that Telegraph was willing to consider required FSLIC to contribute $15,000,000 for 15 years at no interest and for an additional five years at six percent interest. Pet. App. 70. In short, no solution to Telegraph's problems was available without substantial financial assistance from FSLIC (Affidavit of Louis V. Roy at ¶ 5; Affidavit of William J. Schilling at Exh. 2); and no one was willing to acquire Telegraph's business. See Pet. App. 43.

On May 21, 1980, Telegraph's executive vice-president and treasurer wrote to the Illinois Savings and Loan Commissioner stating that operating results for May 1980 would be no more favorable than in prior months. Pet. App. 69-70. Calculations by Telegraph's comptroller showed the situation to be even worse. See *id.* at 68-69. Based on this final confirmation that the financial situation was hopeless, the Illinois Commissioner took custody of the association and closed it. *Id.* at 71. Raymond Bacon, who had been a Telegraph depositor since September 1976, attempted to make a withdrawal, but was unable to do so. *Id.* at 84. Bacon testified that he was asked to attempt the withdrawal because he was a "sophisticated depositor who would understand the consequence of what was going on and not be alarmed unduly by it." Deposition of Raymond Bacon at 37, 53; see Pet. App. 85 n.14.

As a result of the Commissioner's actions, FSLIC was required to meet its insurance obligations to the depositors "as soon as possible." 12 U.S.C. 1718(b). The Bank Board appointed FSLIC as receiver for Telegraph pursuant to 12 U.S.C. 1729(c)(2), deter-

mining that the three statutory requirements necessary for the appointment had been satisfied. Pet. App. 71. FSLIC successfully arranged a "Purchase and Assumption Agreement" with First Federal Savings & Loan Association ("First Federal") pursuant to which Telegraph's depositors received substituted insured accounts at First Federal. FSLIC was required to pay First Federal approximately $178.5 million in cash in return for its agreement to assume deposit liabilities. Affidavit of Gene L. Hall; Affidavit of Carole L. Nelson at Exh. 1; Second Amended Complaint at Exhs. C & D. In return, FSLIC received Telegraph's remaining low-yielding mortgage loans, which petitioners agree were worth at least $30,000,000 less than their face amount. Affidavit of Carole L. Nelson at Exh. 1. As a result of the transaction, FSLIC paid at least $12,500,000 more than it received, but none of the depositors suffered a loss.

3. Petitioners commenced this action in the United States District Court for the Northern District of Illinois challenging the Bank Board's action pursuant to 12 U.S.C. 1464(d)(6)(A). The district court granted partial summary judgment in favor of the Bank Board, concluding that the requirements of 12 U.S.C. 1729(c)(2)(A) and (C) had been satisfied. Pet. App. 84-85. Following a trial, the district court also found that Telegraph was insolvent (its assets were less than its obligations to its creditors and others, including its members). *Id.* at 42. Based on expert testimony, the district court found that the book net worth test of insolvency was a sound standard that had been endorsed by Congress and that fairly identified institutions with critical financial deficiencies. *Id.* at 48-54.

The court of appeals affirmed, concluding that the statutory requirements for the appointment of FSLIC

as federal receiver had been satisfied. Pet. App. 3-23. First, the court of appeals decided that the requirement that a state institution be closed "by or under" state law was met by the undisputed fact that the Illinois Commissioner closed Telegraph on May 22, 1980. *Id.* at 9-12. Based on the language of the statute and its legislative history, the court rejected petitioners' argument that 12 U.S.C. 1729(c)(2)(A) required the district court to decide whether the closing also complied with applicable state procedural requirements. Pet. App. 12. The court noted (Pet. App. 10-11) legislative history stating that the statute was designed "to enable the FSLIC to defend its appointment under Federal law instead of requiring it to defend the legality of the State savings and loan administrator's determinations under State law." S. Rep. No. 1263, 90th Cong., 2d Sess. 11 (1968). Second, the court of appeals rejected petitioners' argument that the closing of an institution is insufficient to establish that "one or more of the holders of withdrawable accounts * * * is unable to obtain a withdrawal of his account * * *" in compliance with 12 U.S.C. 1729(c)(2)(C). Pet. App. 12-15. The court stated that the "inability to withdraw" requirement was added to deal with situations where a state commissioner takes custody of an association for the purpose of operating it. Pet. App. 13-14. When, as here, an association has been closed completely, this requirement is automatically satisfied. *Ibid.* Finally, the court reviewed the evidence and agreed that Telegraph was insolvent, thus satisfying the third requirement for appointment of a receiver. 12 U.S.C. 1729(c)(2)(B). The court also agreed with the district court that the book net worth test of insolvency was both rational and constitutional. Pet. App. 19.

ARGUMENT

The issues raised in the petition were fully considered and correctly decided by the court of appeals. Its decision does not conflict with any decision of this Court or of any other court of appeals. Indeed, it is consistent with the Ninth Circuit's decision in *Fidelity Savings & Loan Association* v. *Federal Home Loan Bank Board*, 689 F.2d 803 (9th Cir. 1982), cert. denied, No. 82-1320 (May 2, 1983).[2] Accordingly, further review by this Court is not warranted.

1. Petitioners contend (Pet. 12-24) that there is an "implicit" requirement, in addition to that imposed by 12 U.S.C. 1729(c)(2)(A), that the federal courts must consider and decide the validity of a state closure under state law. They also contend that failure to consider this question in a suit challenging the Bank Board's appointment of FSLIC as receiver would violate the Due Process Clause of the Fifth Amendment. Petitioners' constitutional challenge has

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[2] In a recent decision in the Southern District of Florida, the district court, although ruling for the Bank Board and FSLIC on four out of five counts, announced its intention to order the receiver (FSLIC) to return an insolvent savings and loan association to its shareholders and ordered the parties to explore means to facilitate such a return. *Biscayne Federal Savings & Loan Ass'n* v. *Federal Home Loan Bank Board*, No. 83-815-CIV-EPS (S.D. Fla. Sept. 9, 1983).

The trial court in *Biscayne* held *inter alia* that 12 U.S.C. 1464(d)(6)(A) and (C) did not preclude the court from reviewing the basis for the Bank Board's decision to appoint a receiver even when the institution involved was admittedly insolvent by more than $29 million. Respondents submit that this holding of the district court is erroneous and conflicts with express statutory language. A notice of appeal has been filed and the Eleventh Circuit has granted an expedited appeal and scheduled oral argument in *Biscayne* for November 15, 1983.

no merit and their statutory construction argument is inconsistent with the Act's express language and its legislative history.

a. Petitioners' only quarrel with the Illinois Commissioner's closing of the institution is that a formal "written notice of intent to assume custody" was not included among the documents served. See Pet. App. 9 n.3. But Telegraph's own Board of Directors minutes show that it received explicit notice on at least three occasions of the Commissioner's intention to take custody unless the financial difficulties were resolved. *Id.* at 12, 69.

Accordingly, even if these state law issues could properly be entertained by a federal court, petitioners' arguments are without merit. More to the point, however, the district court and the Seventh Circuit correctly concluded that such state law issues were not to be adjudicated in a federal challenge to the Bank Board's appointment of a receiver. In this regard, all that the Act requires before the Bank Board may appoint a receiver is a closing "by or under" state law. It is the act of closing—wholly apart from the antecedent procedural steps under state law—that threatens an institution's depositors with loss and triggers FSLIC's obligation to deal with the problem. 12 U.S.C. 1728(b). For this reason, Congress provided that FSLIC would not be required to defend "the legality of the State savings and loan administrator's determinations under State law." S. Rep. No. 1263, *supra*, at 11.

b. Also without merit is petitioners' suggestion that their inability to challenge the State Commissioner's closing in an action under 12 U.S.C. 1464(d)(6)(A) deprives them of property without due process of law. Petitioners were afforded by the federal

courts a full and complete opportunity to challenge the *merits* of the receivership appointment—in this case, whether the Bank Board reasonably determined that Telegraph was insolvent. There is no constitutional right to challenge administrative action twice, once under federal law and once under state law. Nor is there a constitutional right for a plaintiff to select for itself the elements of its cause of action. The savings and loan business, like banking, is "one of the longest regulated and most closely supervised of public callings." *Fahey* v. *Mallonee*, 332 U.S. 245, 250 (1947). Telegraph chose to be governed by federal law and federal receivership standards when it requested and received FSLIC insurance of its accounts. 12 U.S.C. 1726. As the Seventh Circuit correctly observed (Pet. App. 11), the agreement to be governed by federal law is "a trade-off for federal insurance." In these circumstances, petitioners had a full opportunity to challenge the Bank Board's appointment of a receiver. See Pet. App. 12.

c. Petitioners' corollary argument that the cooperation between state and federal regulatory authorities prior to the receivership appointment was in some way improper was squarely considered and correctly rejected by the district court. The court observed that " 'it would be unwise not to get together and coordinate their efforts' " (Pet. App. 65). Given the dual regulatory responsibility of state and federal authorities, such cooperation was essential and was clearly anticipated by Congress. The cooperative effort was openly disclosed to petitioners at numerous meetings of its Board of Directors. Thus, petitioners' criticism of this cooperation is frivolous and was properly rejected.

d. Finally, petitioners' remaining procedural argument—concerning the requirements of 12 U.S.C. 1729

(c)(2)—does not present an important question of federal law that should be decided by this Court, because recent statutory amendments make it unlikely that the issue will recur. In the Garn-St Germain Depository Institutions Act of 1982 (Pub. L. No. 97-320, 96 Stat. 1469 *et seq.*) Congress expanded the Bank Board's independent authority to appoint a federal receiver for state-chartered savings and loan associations. Section 122(d) of the Act, 96 Stat. 1482 (12 U.S.C. 1729(c)(1)(B)), now authorizes the Bank Board to appoint a receiver for a state-chartered institution, without the necessity for a "closing" by or under state law and without the need for a determination whether a depositor has been unable to make a withdrawal. The Bank Board's authority may be exercised immediately if written approval from the appropriate state official is obtained; if such approval is not obtained, the Bank Board must wait 90 days. Under this broad expansion of the Bank Board's authority to appoint a receiver for a state institution, it is unlikely that any of the questions of law raised by petitioners will arise in the future.[3]

2. Petitioners contend (Pet. 26-30) that the decisions below do not accord sufficient significance to the requirement of 12 U.S.C. 1729(c)(2)(C) that a depositor be unable to make a withdrawal. This is inconsistent with the structure of the statute and its legislative history.[4]

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[3] Although these sections of the Garn-St Germain Depository Institutions Act of 1982 are subject to sunset provisions after three years, it is nevertheless unlikely that the language here at issue will be a subject of litigation in the foreseeable future.

[4] Contrary to petitioners' assertion, Subsection (C) of 12 U.S.C. 1729(c)(2) is not the Bank Board's illiquidity requirement. The Bank Board's illiquidity requirement is set forth in 12 U.S.C. 1464(d)(6)(A)(iii) dealing with "an unsafe or un-

The Senate bill as originally introduced contained a "closing" provision, but did not include the "inability to withdraw" or the "fifteen-day custody" conditions. The committee amendment incorporating the two new requirements was intended to provide the Bank Board with authority to deal with an "open" association in custody, a power completely separate from the Bank Board's authority arising when an association is closed. S. Rep. No. 1263, *supra*. Subsection (C) of 12 U.S.C. 1729(c)(2) has important independent significance, confining the Bank Board's intervention to those situations where, despite a State Commissioner's attempt to operate an association, depositors are unable to withdraw their money. The Bank Board's authority upon the closing of an institution is treated earlier in S. Rep. No. 1263, *supra*, but is not mentioned in connection with Subsection (C) because it will always be satisfied automatically upon a closing. Although Subsection (C) was satisfied upon Telegraph's closing, the Bank Board was certainly entitled to rely upon the cautious, alternative procedure of identifying an individual depositor—Mr. Bacon—who was actually unable to make a withdrawal.

3. Petitioners contend (Pet. 24-26) that the courts below erred in applying the statutory insolvency standard as the only substantive requirement for appointment of a receiver and further argue that the book net worth test of insolvency is "irrelevant" in today's economic climate. These arguments are incorrect.

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sound conditions to transact business." Subsection (C) is one of the two state "triggering" requirements identifying situations where FSLIC's involvement will be necessary to protect the depositors of a state-chartered savings and loan association.

a. In enacting 12 U.S.C. 1729(c)(2)(A) and (C) Congress noted that, given the dual regulatory authority over state-chartered savings and loan associations, actions of state authorities will often mean that "FSLIC insurance payments to the savings account holders are automatically triggered." S. Rep. No. 1263, *supra*, at 7. In those instances where FSLIC is required to meet its insurance obligation, Congress granted it independent authority to act as receiver for the institution's assets. Subsections (A) and (C) of 12 U.S.C. 1729(c)(2) identify those situations where state authorities have taken definitive actions that recognize the financial failure of a state-chartered institution and that require action by FSLIC to protect affected depositors. In this case, it was undisputed that the State Commissioner closed Telegraph's offices, making FSLIC's assistance essential.

b. In addition to requirements (A) and (C), which reflect the conclusion of state authorities that a savings and loan is in terminal financial condition, Congress required the Bank Board to reach its own substantive determination under 12 U.S.C. 1464(d)(6)(A) that a receivership appointment is warranted. That section lists five independent requirements, any one of which is sufficient to support the Bank Board's receivership appointment. In the present posture of this case only one of those standards is at issue, whether Telegraph was in a state of "insolvency in that the assets of the association are less than its obligations to its creditors and others, including its members." 12 U.S.C. 1464(d)(6)(A).

The district court heard substantial evidence and found that the book net worth test of insolvency is both rational and reasonable (Pet. App. 48-54). The Seventh Circuit found no basis for upsetting the district court's conclusion. *Id.* at 16-19.

The court's findings upholding the book net worth test of insolvency were strongly supported by the evidence. Savings and loan associations are financial institutions that deal in financial instruments. Their principal assets are mortgage loans that will be repaid dollar for dollar if held to maturity. The book net worth test of insolvency identifies that point at which the assets of the institution would not be sufficient to repay all liabilities, even if the institution's mortgages could be held to maturity and even if no further losses were suffered. The test also identifies the point at which (1) the investment of the owners of the business has been depleted, (2) the investment community loses confidence in the institution, and (3) the members of the public may lose confidence and withdraw their savings (Pet. App. 48-52).

Petitioners' arguments about the insolvency standard do not raise an important question of federal law for the additional reason that Congress has addressed the savings and loan industry's problem of declining book net worth and has decided the extent to which assistance will be granted to the industry. Title II of the Garn-St Germain Depository Institutions Act of 1982 (Pub. L. No. 97-320, 96 Stat. 1489-1496) reflects a recent congressional judgment that book net worth is indeed a valid measure of the financial health of an insured savings and loan association. In light of this current statement of congressional intent, petitioners' arguments are untenable.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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NOVEMBER 1983

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